

5 June 2024

Ms Stephanie Jolly  
Executive General Manager  
Australian Energy Regulator  
Brisbane Qld 4003

By email submission: [RITguidelines@aer.gov.au](mailto:RITguidelines@aer.gov.au)

Dear Ms. Jolly,

**Review of the cost benefit analysis guidelines and RIT application guidelines**

The Australian Energy Market Operator (AEMO) welcomes the opportunity to comment on the AER's cost benefit analysis guidelines and RIT application guidelines review.

AEMO supports the preliminary views reached in the consultation paper relating to the inclusion of emissions reductions benefits, applying the VER in the cost benefit analysis rather than as an input into market modelling (as this better aligns with real-life outcomes), and the carbon budget application complementing the inclusion of the VER.

AEMO considers that the Stakeholder Engagement Plan proposed in the consultation paper should detail an effective and comprehensive engagement process that enables the TNSP to gather the information needed to determine any feasibility risks for RIT-T options. AEMO does not see the need to create new cost or benefit classes for activities to build social licence. We have also provided additional comments on community engagement for RIT proponents.

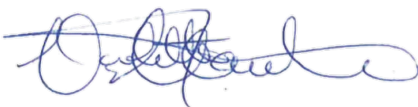
Additional suggestions are provided relating to the appropriate timing for when concessional finance can be deemed likely, and wording amendments in the CBA Guidelines relating to the feedback loop.

AEMO proposes that RIT-T proponents exclude sunk costs from the CBA when selecting the preferred option, but that these costs be transparently documented within the RIT-T.

We have provided some more detailed perspectives on the questions asked in Appendix 1 below.

If you would like to discuss anything further, please contact Kevin Ly, Group Manager – Reform Development & Insights ([kevin.ly@aemo.com.au](mailto:kevin.ly@aemo.com.au)).

Yours sincerely,



Violette Mouchaileh

**Executive General Manager – Reform Delivery**

## APPENDIX 1: AEMO'S VIEWS AND INSIGHTS ON THE CONSULTATION PAPER

This section discusses AEMO's views and insights related to specific questions posed or where views are sought throughout the Consultation Paper.

### Valuing emissions reduction in CBA/RIT

#### *1.1 How should emissions reduction benefits be included in the RIT and cost benefit analysis guidelines?*

AEMO agrees that an emissions reduction class of market benefit should be estimated as the benefit that an investment provides from reducing emissions relative to the base case (where the base case for the ISP is the counterfactual development path and the investment case is the candidate development pathway). The emissions reduction class of market benefit should be calculated as the difference in total emissions in the base case less the emissions in the proposed option, where this difference is then multiplied by the VER and summed across the modelled horizon. This is consistent with the approach we will take in the 2024 ISP .

#### *1.2 Do you have any views on the option to include the VER in the inputs to market modelling as a cost (\$/MWh) on fossil-fuel generators in terms of both its application and the potential outcomes from its application?*

Given that emissions is an impact on society, rather than a cost faced by generators, AEMO does not consider it appropriate to include the VER as an additional cost that informs the dispatch of fossil-fuel generation in market modelling.

#### *1.3 Do you have any views on the implications of the current carbon budget methodology remaining in place at the ISP input stage while the VER contributes to the assessment of the relative net benefit of different development pathways and investment options?*

The ISP adopts a carbon budget approach defined for each scenario to represent the pace of the energy transition to net zero. The carbon budgets are set to be consistent with emissions reduction outcomes (such as emissions reduction pathways consistent with various global temperature rise scenarios – e.g. 1.5°C, 1.8°C, 2.6°C).

The carbon budget is applied as an optimisation constraint for the ISP market models, limiting the available carbon emissions for electricity generation. Depending on the scale of electrification within each scenario, the actions assumed by other sectors of the economy, and the temperature pathways, the carbon budget may lead to a rapid, or more gradual, pace of electricity sector transition.

AEMO considers that it is appropriate to maintain the existing carbon budget approach, to be used alongside the interim value of emissions reductions. The carbon budget approach is an essential tool used to ensure that long-term policy uncertainty is reflected across the scenarios. Additionally, the carbon budget approach is informed by existing policy settings. AEMO considers that the value of emissions reduction applied as the difference in emissions without impacting dispatch complements the carbon budget without double-counting.

AEMO would also like to draw attention to the description made on page 11 of the consultation paper:

*"We note that the current ISP methodology effectively results in a different value of emissions in each development path and each scenario, changing over time and independent of the VER. Under this methodology, emissions may sometimes be indirectly assigned a value that is different to the VER during market modelling, with the purpose of bringing the modelling output emissions trajectory back within the carbon budget".*

The use of carbon budgets as parameters for the ISP scenarios drives down emissions at different paces across the different scenarios. Further emissions reduction therefore has a different economic cost in the different scenarios. These scenarios are used to provide a range of future worlds to assess the different pathways to net zero and therefore the robustness of the optimal development path against these potential future worlds. The VER is applied in a different way in the ISP methodology in that it is only applied to the evaluation of transmission projects. For each scenario in the ISP both the development path and the counterfactual are driven down to the carbon budget. This means that the emissions benefit for the development path is dependent on whether it brings forward emissions reduction ahead of the counterfactual or naturally reduces emissions further than the budget. The difference in emissions between the development path and the counterfactual is multiplied by the VER to calculate the emissions reduction benefit. Therefore the shadow price of the carbon budget doesn't directly influence the emissions benefit of the transmission projects.

*1.4 Are there alternative approaches to estimating an emissions reduction benefit, and if so, what are the advantages and disadvantages of alternative approaches that should be considered?*

*1.5 Which additional material factors should be considered in modelling emissions? How should data to support these factors be sourced? Should the AER consider including specific guidance on any of the factors?*

The ISP currently considers what is defined as 'Scope 1' by the National Greenhouse and Energy Reporting Scheme (NGERS)<sup>1</sup>, which is "direct" emissions. Scope 2 and Scope 3 emissions are currently out of scope. AEMO considers that the application of Scope 2 and 3 emissions could bring significant uncertainty and complexity to the assessment and may not be material to the overall outcomes. In the event these are considered for inclusion it would be appropriate for guidance regarding their calculation to be developed ahead of the requirements.

The discount rate and time series trajectory of the VER influences the relative cost of early or late emissions reductions. A higher discount rate increases the relative value of early emissions reduction, by increasing the relative discount of later years as compared to early years of the modelling horizon. Similarly, higher discount rates increase the relative costs of early infrastructure investments which require early capital investments. AEMO considers that emissions reduction should be considered consistent with other system costs, via discount rate interaction with the CBA. The VER trajectory should be set with the understanding that the costs will be discounted under the CBA approach.

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Clean Energy Regulator, National Greenhouse and Energy Reporting Scheme, at: <https://cer.gov.au/schemes/national-greenhouse-and-energy-reporting-scheme>

## **Social Licence - Identifying credible options in a RIT-T assessment**

2.1 *What factors or criteria should a RIT-T proponent consider when determining whether a project:*

- *is going to be delayed, or is not likely to proceed such that the project is no longer technically feasible?*
- *is not likely to be delivered in sufficient time to meet the need?*

2.2 *What might be some objective measures of any factors identified above?*

2.3 *If initial community engagement indicates that an option may not be credible, what further engagement or other action should a transmission business undertake to determine if an option may later become credible?*

AEMO considers that the Stakeholder Engagement Plan proposed in the consultation paper should detail an effective and comprehensive engagement process that enables the TNSP to gather the information needed to determine any delivery risks for RIT-T options. The TNSP could use a risk-based approach to assess the likelihood of each project option being infeasible and remaining infeasible based on evidence collected during stakeholder engagement. The TNSP should draw on quantitative evidence where available, but also be informed by qualitative evidence of risks to project delivery.

Proponents should give consideration to independent, credible research, such as the CSIRO's Australian Attitudes to the Transition report, to inform their assessments of local community sentiment.

AEMO is of the view that the *Bringing early works forward to improve transmission planning*<sup>2</sup> rule change, part of which allows TNSPs to undertake early works activities and request a Contingent Project Application concurrent with the RIT-T, should assist in TNSPs being able to undertake early works activities which can influence both the social licence and the consideration of credible options. The current RIT-T consultation process can be likened to a Decide, Announce, Defend approach, which has the potential to feel very dismissive for communities. In contrast, undertaking stakeholder engagement either before or concurrently with the RIT-T should increase TNSPs ability to build trust with the communities, and create a shared vision that aligns with their values and expectations. It will also enable TNSPs to provide improved information to AEMO to factor into the earliest in-service delivery date that is assumed for each project in the ISP.

## **Social Licence - Costs and market benefits in ISP and RIT-T assessments**

2.4 *Is there a need to clarify costs and benefits that may be included in the RIT-T to address social licence issues? What worked examples would be useful?*

2.5 *Are any additional classes of costs and market benefits necessary to address social licence issues, and available within the framework provided by the Rules?*

2.6 *How could the effect of delays on the costs and market benefits of each credible options be assessed and justified?*

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<sup>2</sup> AEMC, Bringing early works forward to improve transmission planning, at: <https://www.aemc.gov.au/rule-changes/bringing-early-works-forward-improve-transmission-planning#:~:text=Early%20works%20describe%20activities%20such,planning%20approvals%20and%20easement%20acquisition>

*2.7 If a RIT-T were to include forecast expenditure on social licence activities to address an identified reduction in market benefit due to project delay, what justification would be required to demonstrate this expenditure will reduce the potential project delay?*

AEMO considers that the costs incurred to undertake comprehensive community engagement and to implement activities to build social licence could be assessed as part of a RIT-T under the existing classes of costs and benefits. AEMO does not see the need to create new cost or benefit classes for activities to build social licence. However, greater clarity on what can and cannot be considered in assessing these costs may be beneficial, noting that there is no 'one size fits all' and practices need to be tailored to what is likely to be most suitable for the relevant community associated with actual projects. Therefore any examples need to recognise these requirements will change between projects and over time as engagement practices evolve in response to experience. It should also be noted externalities are not currently permitted.

The AER's approach to assessing proposed expenditure on social licence activities should be sensitive to the challenge of attempting to quantify the achievement of social licence, a deeply intangible and complex concept. The assessment approach should be flexible and tailored to the project/community context and the stage of the project. While RIT-T proponents could put forward a risk-based analysis of the merits of proposed expenditure on social licence activities, this may focus on investing up front to avoid risks of future costs during construction which are unlikely to be entirely quantifiable and may rely on qualitative judgements. For example, a detailed assessment of costs associated with minimising any adverse project impacts for landowners will not be known until a route has been selected, and TNSPs have had opportunity to gain a detailed understand of how the land is used. Also the approach to community engagement will need to be flexible enough to respond to what response occurs and this will continue to change throughout the development and delivery of the project.

### **Social Licence - Community engagement - Enhancing community engagement in transmission building**

*2.8 There are several areas of the Guidelines for which clarification may be provided following the updated definition of 'interested party'. We are seeking stakeholder feedback around the provision of these clarifications.*

*2.9 We are also seeking views on whether the Guidelines should be prescriptive about these matters or should set out principles within which RIT-T proponents should operate.*

*2.10 The definition of stakeholders that are "reasonably expected to be affected by the development" of the project*

- *What criteria should be used to establish when a stakeholder is 'reasonably expected' to be affected? Are there conditions to consider other than the presence of a stakeholder group in the geographical area of a project?*
- *What threshold should be considered when assessing whether a stakeholder is 'reasonably expected' to be affected? To what extent are RIT-T proponents able to assess the materiality of effects on stakeholders before engaging with them?*

*2.11 How should interested parties be identified?*

- *Should reasonably affected stakeholders be identified nominally, by constitution of a list in advance?*
- *Should RIT-T proponents identify specific affected stakeholders, or rather ensure that the consultation addresses each category of stakeholder?*
- *Is it necessary or sufficient to have representation of each category of stakeholders?*

AEMO considers that the AER should draw on the views of TNSPs and recently developed resources such as the impending DCCEEW National Guidelines for Community Engagement and Benefits Sharing in response to these questions.

### **Social Licence - Community engagement - Planning stakeholder engagement**

- 2.12 *While community engagement expectations require that “reasonable endeavours” should be used, how should this be interpreted and what would be the minimum expectations for tailoring engagement materials and communication methods to meet the needs of different stakeholders?*
- 2.13 *The community engagement expectations include that “stakeholders (will be) provided with a range of opportunities to be regularly involved throughout the actionable ISP projects, future ISP projects and REZ stages”. Should there be guidance on what opportunities for regular involvement the RIT-T proponent could consider providing stakeholders with?*
- 2.14 *What requirement should the guidelines contain for a RIT-T proponent to publish an engagement plan on how it will make reasonable endeavours to satisfy community engagement expectations?*
- 2.15 *How can we promote continuity and avoid duplication between AEMO’s engagement work, and the engagement undertaken by the RIT-T proponents?*

AEMO recognises that many TNSPs are already undertaking stakeholder engagement and have committed to better engagement principles. The forthcoming DCCEEW National Guidelines for Community Engagement and Benefits Sharing will be an additional resource to guide best practice.

AEMO agrees that RIT proponents should be required to develop a detailed stakeholder engagement plan for major ISP projects. In the stakeholder engagement plan, the RIT proponent should explain how the actions proposed complement and avoid duplication with engagement undertaken as part of the ISP process.

The current CBA guidelines state that proponents ‘must consider undertaking early engagement only to the extent that doing so complements rather than duplicates or hinders AEMO’s engagement work in developing the ISP.’ In practice there is unlikely to be overlap or duplication, given the differing level of engagement activities that AEMO and TNSPs undertake.

### **Social Licence - Community engagement - Engagement on draft and final reports**

- 2.16 *For the draft and final reports, is the normal means of consultation (by publication on proponent and/or AEMO website) sufficient to be in accordance with the expectations?*
- 2.17 *What should we require proponents to include about stakeholder feedback in the draft and final reports?*

Proponents should detail in their stakeholder engagement plans how they intend to engage with community during the process as well as how they intend to respond to stakeholder feedback. These documents are necessarily technical in nature and currently targeted at industry engagement. Additional elements need to be included for effective community engagement. TNSPs need to be provided flexibility as to what will be most effective for the given project and communities involved. At a minimum, the final reports should provide a summary of how stakeholder feedback has been considered in the decision-making.

For the VNI West project, AEMO Victorian Planning and Transgrid released an Additional Consultation Report in February 2023, which reflected feedback received in submissions to the Project Assessment Draft Report (PADR). AVP and Transgrid held a series of webinars and deep dives to engage with stakeholders on the Additional Consultation Report and published responses to the questions raised in those sessions.

Subsequently, the Project Assessment Conclusions Report (PACR): Volume 2 summarised all the points raised in the Additional Consultation Report submissions, explained how they were taken into account in finalising the PACR and outlined engagement activities undertaken by AVP and Transgrid up until that date. Consideration of the issues raised by stakeholders in relation to both the PADR and the Additional Consultation Report played a pivotal role in the finalisation of the VNI West PACR.

### **Sharing concessional finance benefits with consumers**

*2.18 What evidence of the likelihood of a concessional finance agreement being put in place would be necessary before a RIT proponent can or should account for the effect of the concessional finance on the capital cost of credible options?*

AEMO considers that a memorandum of understanding or a signed letter from the GFB would be sufficient evidence to prove the concessional finance is likely to occur.

*2.19 Are there non-confidential details of a concessional finance arrangement that a proponent should and could provide in their report?*

*2.20 Are there any specific areas that the AER could clarify using worked examples?*

### **Improving the workability of the feedback loop**

*3.1 We welcome stakeholder views on the proposed amendments to reflect the AEMC's final rule on improving the workability of feedback loop.*

AEMO supports the intention by the AER to provide guidance on the timing of a feedback loop request to effectively create an 'exclusion window' for feedback loop assessments in the period between the publication of the final IASR and the publication of the draft ISP, with AEMO retaining the discretion to undertake the assessment during this time where appropriate.

The Guidelines should clarify that TNSPs should contact AEMO if they believe that the circumstances of a particular feedback loop request might warrant assessment during the exclusion window, for example for less complex projects where remodelling might not be required. This approach would ensure that, where appropriate, feedback loop assessments can be progressed to avoid unnecessarily delaying ISP projects from being built according to the optimal timing as outlined in the ISP.

## Early works contingent project application before completion of a RIT-T

### 4.1 How should early works costs already incurred, or committed through a contingent project determination, be treated in a cost-benefit analysis in a RIT-T?

Whilst the consultation paper focuses on the RIT-T, we would like to highlight the importance of ISP/RIT-T alignment. As required by the NER and current CBA Guideline, inputs and assumptions should be aligned unless there is a demonstrable reason for them to depart. The approach that AEMO takes for the ISP and feedback loops treats incurred costs as sunk unless they can otherwise be resold. This is consistent with Infrastructure Australia's guide to economic appraisals.

Consumers bear the costs of both the early works CPA and the remaining RIT-T CPA. If including sunk costs in the RIT-T changes the preferred option, then consumers would pay for all sunk costs, in addition to all costs for the newly preferred option that is, the total cost paid by consumers would be the full cost of the newly preferred option plus the sunk costs of the previous preferred option. Unless the net benefits of the newly preferred option (including sunk costs as part of total cost) are greater than the net benefits of the previous preferred option (including sunk costs), consumers would be worse off from a change in option. Consumers should be able to benefit from the decisions already made in the early works CPA. As an example, consider an actionable ISP project for which the early works involves strategic easement acquisition<sup>3</sup>. Following the completion of the RIT-T the TNSP identifies that it would have been better originally if the TNSP acquired a different easement, but given customers have already paid for the original easement, they would continue with the easement they've already purchased. AEMO does not consider it appropriate to make investment decisions ignoring the sunk costs that have been made. The decision should be based on what is in the consumers best interest going forward.

Certain costs approved in early works may be recoverable and should not be considered as sunk. For example, if in early works electrical equipment is purchased, that equipment has a resale value and can be resold if they are not needed for the RIT-T preferred option.

Although we propose RIT-T proponents exclude sunk costs from the CBA, they should be required to transparently document these costs in the RIT-T.

Further, we would like to ensure consistency between the approach to incurred costs, and the existing approach to staging projects. The CBA Guidelines cites a specific example of a project staged in the ISP, "*where early works would be 'Stage 1' of a staged project, and 'Stage 2' would be to build the interconnector*". In this example, once the AER has approved the CPA for stage 1 early works, AEMO would typically treat that project as "anticipated" for the purposes of subsequent ISPs as it is sufficiently advanced to meet the definition. If the subsequent ISP identifies stage 2 as actionable, the stage 1 early works costs will be considered sunk given it is treated as an anticipated project. The position outlined in the consultation paper would therefore create an inconsistency with this approach, despite the logic being consistent. AEMO supports the current approach to the treatment of sunk costs for staged projects in the ISP and believes consistency with this approach would be appropriate.

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<sup>3</sup> We note that the current draft determination of the [Bringing early works forward to improve transmission planning](#) rule change includes principles which appear to potentially exclude activities which are not common across all options from the definition of early works, but use this example to highlight the flaws of incurred costs being included in selecting the preferred option in the RIT-T given the potential for the final determination to expand the scope of early works, which would mean this would have a material impact on selection of the preferred option.